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I. CHINA: DENG AGAIN PUTS HIS STAMP ON POLICY AND POLITICS
(11/4)

Deng Xiaoping seems to once again to be playing an active, albeit episodic, role in PRC politics and policymaking. He reportedly has had a moderating influence on recent foreign policy, particularly toward the United States and the Soviet Union, but his intervention on personnel issues and efforts to accelerate economic reform could boomerang.

Foreign policy activism. Deng's steady hand has been especially noticable in foreign policy.

According to several accounts, Deng has intervened to prevent further deterioration of relations with the United States.

Shaking things up. Deng has used the failed Soviet coup as a springboard to push for more rapid economic reform, arguing that the Party's standing with the public is determined by China's economic performance.

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Running a risk. Younger leaders resent Deng's chiding:

Deng's pressure in 1986 for Hu Yaobang to be named military commission chief precipitated a crisis, as did his ill-timed demands for more rapid action on price reform in 1988, an incident that worked to the disadvantage of Deng's then-chosen successor Zhao Ziyang.

Younger leaders probably will be more hesitant to respond to Deng's importunings this time around, but excessive pressure by an old man in a hurry for controversial policies or personnel changes runs the risk of setting off another leadership crisis. (SECRET/NOFORN/NOCONTRACT/ORCON/EXDIS) (CClarke)

II. CHINA: LOYALTY, NEPOTISM, AND THE SUCCESSION (10/23)

Chinese leadership shock over Soviet political turmoil appears to have derailed at least temporarily, Deng Xiaoping's newest plan for an orderly succession. Deng had hoped to engineer the promotion of like-minded reformers, but personnel changes at the central committee plenum expected in early November probably will be minimal. Many party elders are pressing for the promotion of their children to top posts, including the central committee, a step sure to rekindle anger over nepotism within the party and in the public at large.

Beijing has not announced the date of the long-overdue eighth plenum, but travel plans by top leaders suggest it may be held on or about November 10. The plenum's agenda remains murky, with rumors suggesting agricultural and water conservation policies could be a focus, along with China's place in the world and the sad state of China's state enterprises. Some leadership changes are almost certain in preparation for a full party congress next year, but high-level wrangling may keep personnel changes to a minimum and relatively non-controversial.

Status quo at the top. Leaders reportedly are discussing the possible retirements at or after next year's congress, of Advisory Commission Chairman Chen Yun, President and Military

Commission Vice Chairman Yang Shangkun, and other still-active elders. Yang's retirements would clear positions for younger leaders, but Deng would still count on Yang to smooth the succession after Deng dies. The plenum is unlikely to telegraph these very controversial changes.

Leaders are also wrestling with whether to "elect" Premier Li Peng to another five-year term in early 1993; Li and his supporters are said to be actively lobbying for his retention, while [REDACTED] others are pushing for his replacement by either Vice Premier Zou Jiahua or Vice Premier Zhu Rongji.

Neither Zou nor Zhu is on the politburo--Zhu is not even a central committee member, an unprecedented situation for a vice premier. Both will almost certainly join the politburo at the plenum [REDACTED]

...and keeping it in the family. Chastened by the Tiananmen and by the collapse of the Soviet Communist party, top leaders reportedly have concluded that the future of their regime lies in the promotion of their own children, the only younger leaders they believe they can trust and control. The politburo is said to have ordered lower levels to identify promising candidates for elevation at next year's congress, judging them on experience, work performance, education, political reliability, and stand during the Tiananmen crisis.

Military, scientific, and provincial representation on the central committee is to be boosted, and lower levels were told especially for children of party veterans with proper qualifications. [REDACTED]

Neuralgia on nepotism. Nepotism and official corruption, often linked in China, were among the top complaints of protesters during the 1989 Tiananmen demonstrations. Wholesale promotion of high cadres' children to top positions will only further erode regime legitimacy and increase the likelihood of post-Deng political turmoil. Anxious and running out of time, however, party elders may believe promotion of their children is the only way to assure their legacy is not quickly overturned after they are gone. (SECRET/NOFORN/NOCONTRACT/ORCON/EXDIS) (CClarke)

III. CHINA: TRIMMING THE BUREAUCRATIC FAT (10/29)

With the Chinese budget deficit at a record level and still climbing, Beijing is again trying to pare back its bloated, inefficient, and costly bureaucracy. Since 1978, several efforts to trim the fat have failed--indeed, personnel growth

accelerated in the 1980s--casting doubts on the prospects for the current attempt. Moreover, reformers' hopes to link bureaucratic streamlining with civil service reform, largely on hold since Tiananmen, are likely to run afoul of hardliners' demands for political loyalty among government workers.

With revenue growth sluggish, large and growing government spending to underwrite money-losing state enterprises threatened to push China's budget deficit to record levels even before last summer's devastating floods required massive immediate outlays. Leadership concern over Beijing's strained coffers have helped revive a number of reforms, including a new effort to reduce the bureaucracy.

Organizational bloat. Beijing first faced the issue of bureaucratic overstaffing in the early 1980s; the return of those purged during the Cultural Revolution dramatically increased the government payroll because few existing employees were fired. Since then, the growth of parallel planned and market-oriented economies has spawned numerous new agencies; decentralization of power resulted in a proliferation of local offices to manage and coordinate affairs formerly handled in Beijing; and political competition has led to creation of competing think-tanks and ad hoc institutions.

A costly problem... Nationwide, China now has more than 33 million public employees, according to official press. The number of national and provincial officials nearly doubled from 1979-89, with a million college graduates and military veterans joining the government yearly while only 400,000 people retire. Officials estimate the cost of each bureaucrat to the state as about equal to the net annual income of ten peasants. State administrative expenditures nearly quadrupled during 1979-89, while state income barely doubled. As a share of total government spending, administration roughly doubled during the same period.

...with little hope of solution. Top leaders are devoting personal attention to trimming the fat. Premier Li Peng heads a new Central Organizational System Commission designed to centralize control over personnel structure, staffing levels, and personnel policy. Li reportedly has imposed a freeze on hiring or creating new agencies. Vice Premier and State Planning Commission Chairman Zou Jiahua heads a new Job Allocation Reform Commission which apparently will be tasked with coordinating personnel and civil service reforms and streamlining efforts. Party chief Jiang Zemin reportedly wants the issue of personnel reform placed on the upcoming party plenum's agenda.

Statements of intent notwithstanding, past experience suggests Beijing will have little long-term success controlling the growth of bureaucracy. The center has few ways to enforce its will over localities, and local governments have powerful

incentives to expand their span of control over resources and business. Moreover, plans to trim the bureaucracy, at least at the central level, are likely to become hostage to struggles between reformers who advocate non-political criteria for employment and hardliners who insist on removing "bourgeois liberals" and appointing the "red" over the "expert."
(CONFIDENTIAL) (CClarke)

IV. CHINA: USING THE PAST TO SERVE THE PRESENT

Chinese leaders, in commemorating recent historic anniversaries, have manipulated nationalistic themes to bolster the communist party's sagging legitimacy and underscore its importance to modernizing China. In an October 10 speech celebrating the 80th anniversary of Sun Yat-sen's "bourgeois revolution" against the Manchus, President Yang Shangkun adopted a decidedly reformist tone on domestic affairs, while excoriating those who would obstruct the "righteous cause" of China's unification. Patriotic rhetoric has wide appeal among older Chinese--at home and abroad--but younger generations probably will find little resonance or relevance.

Throughout the 1980s, as Beijing deemphasized ideology, it increasingly invoked patriotic themes to bolster regime legitimacy, especially in times of domestic trouble or deteriorating foreign relations. Tiananmen and the death of Leninism in the Soviet Union and Eastern Europe added new urgency to leaders' efforts to convince the public China can and must retain socialism and party rule.

Party history. Party chief Jiang Zemin's July 1 speech commemorating the 70th anniversary of the communist party's (CCP) founding has been trumpeted as a major policy statement requiring nationwide study. Its theme--the historical inevitability of the party's role in overthrowing feudalism and imperialism and in modernizing China--has received extensive media treatment. Leaders also have underscored the failure of earlier regimes to safeguard China's national interests through widespread propaganda focused on the anniversary of the 1840-42 Opium War, the 1931 "Mukden Incident" which initiated Japan's takeover of Manchuria, and the 110th birthday of China's most famous writer, the leftist Lu Xun.

"Double Ten". Yang's speech celebrating the October 10 ("Double Ten") 1911 revolution--sacred on both the mainland and Taiwan--used history to tout reform. Yang praised the "great contributions" made by "bourgeois revolutionaries" like Sun and gave pride of place to the nationalistic goal of increasing China's wealth and power over the ideological goal of building communism. Said Yang, "every Chinese, irrespective of his or her status in society, party affiliation, or religious belief"

can and should support the patriotic goal of modernization. The "fundamental thing," said Yang, is to promote the economy, and other matters should be subordinate to this task.

China's past economic and social successes, according to Yang, stem from adopting socialism; its ability to "stand firm amid a changing international situation" is the result of the "achievements of reform and openness." Despite the risk, "stopping or rolling back" reform can lead only to a dead-end. Yang even held out the prospects of future political reform, saying that once China becomes prosperous, "we will have more leeway to deal with various complicated situations."

Yang the new arbiter? The authoritative and programatic tone of Yang's speech, delivered while flanked by party chief Jiang and Premier Li Peng, suggests Yang in some respects have already replaced Deng as final arbiter. Yang was very frosty toward advocates of Taiwan independence--"foreign" as well as Chinese--but overall, his speech places him firmly in the camp of those favoring economic reform while holding out the prospects for some future political relaxation (CONFIDENTIAL) (CClarke)

V. PRC/US: STRATEGY FOR HANDLING "301" TRADE DISPUTE. (10/19)

Beijing is taking an unflustered approach in responding to US demands for freer market access and better intellectual property protection. Moderates, who hope to use the "301" dispute and GATT accession process to advance reform, are being challenged by bureaucrats with a strong vested interest in maintaining protectionist barriers. After gauging US resolve and priorities, Beijing probably will time its response to the 301 investigation to undercut US opponents of MFN extension, hoping as well to revive the PRC's-and slow down Taiwan's-GATT bid.

Despite Beijing's public rejection of Section 301 charges of unfair trade practices, its private response has been mild. A USTR delegation arrives in Beijing October 21 for another round of talks. China's response accords with Deng Xiaoping's injunction to mend fences and keep a low profile.

Using the process. Beijing no doubt hoped its [REDACTED] response to USTR [REDACTED] would forestall a Section 301 investigation. Since it didn't, PRC leaders will seek to use the investigation process to obtain several Chinese goals. By showing at least minimal good faith in "301" talks, they hope to derail efforts to revoke China's MFN status.

They hope to craft a package of responses that will satisfy US concerns, and will seek assurances they will not have to renegotiate the same issues in the GATT context. They hope

concessions will unblock China's GATT application, thereby undercutting Taiwan's claim it should not be required to wait for simultaneous admission with a laggard PRC. Leaders may also hope concessions on trade and transparency will repair damage to China's reformist aura and deflect human rights criticism.

Lining up the ducks.

[REDACTED] 91

When the administration rejected China's offers as insufficient, the moderates lost face. Powerful opponents of opening the system further to foreign competition, including planning and heavy industrial ministries, probably cannot be bypassed [REDACTED] Though Chinese negotiators stress the strength and conservatism of their opponents to convince Washington to curb its objectives, additional concessions will have to be hammered out internally, with moderates not only fighting off bureaucratic opposition but having to protect themselves against charges of selling out China's interests, kowtowing to foreign pressure, and subverting socialism. 6.

Outlook. China's economic conditions favor some progress on trade problems: foreign exchange reserves are at a record high, the domestic economy is temporarily stable, the leadership is beginning to grapple with forcing state firms to be more efficient, and proponents of reform are becoming more assertive. Imports this year are beginning to recover after last year's cutbacks and could total \$61 billion, compared to \$53 billion last year. The US share of the China market, however, continues to diminish.

Beijing will move cautiously; China's leaders repeatedly have expressed concern that their concessions are undervalued by the United States and only result in additional demands.
(SECRET/NOFORN/NOCONTRACT/ORCON/EXDIS) (INR/EC:WNewcomb)

VI. TAIWAN/PRC: THE POLITICS OF INDEPENDENCE (10/16)

Taiwan's most important opposition party has crossed the Rubicon by openly calling for independence. Despite pressure from Kuomintang (KMT) conservatives and Beijing to take strong

action against the Democratic Progressive Party (DPP), ruling party leaders will be reluctant to do so for fear of upsetting political stability, provoking street protests, and derailing democratic reforms.

KMT leaders probably judge that the current DPP--weighted toward radicals advocating independence--is not a threat to continued KMT rule. Defeating the DPP at the ballot box will stabilize the political situation to the benefit of the KMT; suppression of the DPP can only lead to tension and uncertainty.

On October 13 the DPP amended its charter to make advocacy of Taiwan independence a party goal. Though a moderate was elected chairman, control of the central executive committee and standing committee passed from moderates to radicals, who believe, probably mistakenly, that the new pro-independence stance of the party will increase its support in December national assembly elections.

Based on past experience, DPP leaders expect the KMT to react mildly, and to placate the KMT they have softened the call for independence by making it subject to a plebiscite. DPP party leaders say they are prepared to form a new opposition party immediately if the government disbands the DPP.

Kuomintang Options. While condemning the DPP as irresponsible and endangering Taiwan's security, the KMT initially has reacted cautiously by calling for an investigation to determine whether the DPP has broken sedition or civic organization laws, which prohibit advocating separatism. Depending upon legal findings, the government could either warn or disband the DPP or, conceivably, arrest selected leaders.

Despite pressures from conservatives and from the PRC to crack down on the DPP, the KMT faces constraints that suggest a more moderate course. For reforms to have meaning, the KMT has to have a political opposition. Disbanding the DPP in the run-up to December 21 national assembly elections would undercut the legitimacy the KMT is trying hard to establish.

Bringing the independence issue out into the open and resolving it politically--through debate and the ballot box--may help defuse the controversy surrounding a previously forbidden topic. Confident of victory in December, the KMT should feel comfortable facing the independence issue politically. Advocating independence may weaken the DPP by driving off moderate supporters.

PRC Reaction. Independence activism in Taiwan has followed naturally from political reform and has heated up considerably with the approach of December elections. In reaction, the PRC has increasingly condemned Taiwan independence and threatened it will not allow the movement to succeed. But its principal

strategy is to put pressure the KMT to take stronger actions than merely issuing anti-independence statements. By putting pressure on the KMT, it can hope to worry the Taiwan electorate sufficiently to reject independence and force the DPP to tone down its demands. Beijing knows the DPP is a minority, that Taiwan public opinion is against independence, and that independence is not a real threat at this time. (CONFIDENTIAL) (MFinegan)

VII. PRC/HONG KONG/UK: DEMOCRATIC CHALLENGER (11/4)

China's send-off blast at Legislative Council (Legco) member Martin Lee, who will be visiting Washington this week, again illustrates that Beijing's tough post-Tiananmen line toward Hong Kong has produced decidedly mixed results. Conservative local and foreign businessmen are adjusting to the prospect of PRC rule in 1997, but China's pressures are building significant popular resentment.

Popular support for Tiananmen student demonstrators in 1989 and later raised PRC fears that Hong Kong would become a base of subversion. China shook up its Hong Kong apparatus, took a tough line with the British and Hong Kong government, and attempted to shift the focus of its attention from "unreliable" upper classes to the masses, claiming that China best represented the will of the Hong Kong people. Negotiations with the British ground to a halt, particularly over the controversial airport project. Bewildered by Beijing's inconsistent mix of tough talk and reassurances, many in Hong Kong became suspicious of China's intentions.

All sides saw a better situation earlier this year after the resolution of the airport controversy, the visit of Prime Minister Major, and renewed progress in negotiations with the British. But the September Legco elections were a major setback to Beijing. Not only did pro-democracy liberals--notably Martin Lee--resoundingly defeat pro-PRC candidates, they won in the face of strong PRC opposition.

Distaste for Martin Lee. Martin Lee is Beijing's bete noire for leading the Hong Kong alliance in support of the democracy movement in China. The Chinese have repeatedly indicated they will not allow him to sit in the post-1997 Legco unless he mends his ways. In 1989 the Chinese expelled Lee from the Basic Law drafting committee because of his outspoken support for the student demonstrators, and Lee has since criticized the Basic Law for not protecting Hong Kong against PRC interference.

Under the Basic Law, China will control senior appointments in Hong Kong and reserve powers that allow it to intervene virtually at will.

Hong Kong Politics: Political parties are embryonic in Hong Kong and so far the only real contest has been for a minority of seats on the Legco. China--preferring a strong executive system under PRC control, after 1997--is determined to keep it that way, and the British may be content to go along.

Despite the impressive victory of Lee and other United Democrats of Hong Kong (UDHK) candidates in the Legco elections, the Hong Kong governor has not appointed UDHK members to the appointed seats in Legco or to the cabinet-like Executive Council (Exco). Because the UDHK refuses to play by the rules of confidentiality of Exco deliberations, the governor had an easy choice. If Lee and the UDHK increase their strength in 1995 elections, the British and the PRC will face a greater challenge. (SECRET/NOFORN/NOCONTRACT/ORCON/EXDIS) (MFinegan)